F I N A L D R A F T

Inclusion of Capital Outlay Revenue Limit and Soft Capital Allocation to the Existing M&O Sudden Growth Formula Calculations.

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HISTORICAL BACKGROUND

Prior to 1980, the State of Arizona had a separate Tax Levy for Arizona School Districts. Each district was allowed to implement a Capital Outlay Levy amount of $ 0.30 and a Capital Levy amount of $ 0.60. There were no budget limits, which meant the full amount of each district's levy was entirely dependent upon its assessed valuation. Wealthier districts with a large tax base could levy a large amount of capital money, while other districts struggled to raise even a modest amount. The resulting inequities between districts were significant.

In the early 1980's the Arizona Legislature refined its School Finance System to provide equal dollars per pupil for school operations through a balancing of the local qualifying Property Tax Rate and State of Arizona Financial Assistance. This concept, commonly referred to as the "equalization formula" allowed public school districts throughout the state to experience a similar "effort" in raising educational dollars for their students regardless of the value of property within their boundaries. This equalization formula is used to calculate a district's <u>Revenue Control Limit</u>, <u>Capital Outlay Revenue Limit</u>, and its <u>Soft Capital Allocation</u>. Over a five year period, the equalized funding formula brought high wealth districts down by approximately 20% and low wealth districts up 20%. The Legislature later created the Capital Outlay Revenue Limit (CORL) and Capital Levy Revenue Limit (CLRL) monies to replace the old Capital Levies. The formula was supposed to increase annually to account for inflation, but for several years there were no increases.

In 1984, districts were allowed to transfer money from the Capital Outlay Revenue Limit Funds into the M&O Budget to help increase teacher salaries and pay for other maintenance and operations costs. This worked well for districts until the 1990's. During this time, the state legislature discontinued funding the budget formula as it had in the past. This action resulted in Districts moving more and more of the CORL Funds into M&O. The movement of these capital funds was then offset by proceeds from Bond and Capital Override elections. Once again, wealthier districts generated large sums of money for pennies on the tax rate; while tax rates in lower wealth districts increased significantly, (assuming a majority of the electorate would even approve the ballot initiative).

In 1994, the Arizona Supreme Court ruled that the state's statutory formula for funding school facilities and equipment violated the Arizona constitution. A four-year struggle to create a new capital finance system ended in July 1998 when the legislature passed and Governor Hull approved SB 1101, a revised version of Students FIRST *(Fair and Immediate Resources for Students Today)* legislation. Students FIRST created a completely new capital financing system aimed at creating minimal adequacy standards for capital-related issues in public schools. This new system would be a more tightly-controlled capital funding system than provided for in the past (typically financed by the sale of general obligation bonds), and it would be governed by a new governmental entity called the School Facilities Board (SFB).

In 1998, the Capital Funding language changed and the newly-formed SFB created the Unrestricted Capital Fund, the Soft Capital Fund and other capital funds to account for SFB projects. The Unrestricted Capital Fund was used like the CORL Funds of previous years and could be moved into the M&O Fund. Again, many districts continued to transfer a large portion of this fund into M&O to offset the on-going costs of operating its schools.

Also during the 1990's, the legislature changed the laws allowing school districts to increase its current year budgets to account for student growth. Since the district's Base Support Level and Revenue Control Limit for the current budgetary year is calculated using the prior year's 100th day ADM, the new law read that if the current budgetary year's ADM is greater than the prior year's 100th day ADM, a district may revise its budget upward by the increased ADM (Group A Category). Adjustments were also allowed in the Group B Category. (ARS 15-948)

THE DILEMMA

The new law has helped growing districts; however, Capital Funding was not increased with the sudden growth formula and could not be increased in the current fiscal year. Instead, if a district experienced student growth greater than 5% over the prior year 100th day ADM, it could increase the calculated Capital Outlay Revenue Limit by the actual percentage increase in the school district's student count in the next fiscal year. This has placed a current year budget burden upon growing districts, representing nearly half of the districts in the state.

As an example, a district of 10,000 students growing at a rate of five percent in one year would increase by five hundred new students, or what could be the equivalent of an entire new school. The district would then need to provide, in addition to approximately 20 new teaching positions, additional capital items such as textbooks, instructional supplies, teacher computers and phones, desks, chairs and student computers. As a way of rectifying this problem, growing districts are using a portion of the funding designed to be used for returning students to cover the cost of capital items needed for new students. This problem is compounded exponentially by districts with growth rates higher than the five percent used in this example.

FISCAL IMPACT

The share of the State of Arizona's General Budget designated for funding sudden growth would increase by including Capital Outlay Revenue Limit and Soft Capital Allocation to the existing M&O sudden growth calculation. However, the elimination of the five percent factor included in the current Capital Outlay Revenue Limit calculation would reduce the amount required.

Committee member (and Interim Director of Operations for Arizona Department of Education School Finance Unit) Bonnie Betz analyzed the fiscal impact to the state budget. Her analysis shows that the cost of funding capital growth, based on FY05 data, would be a net $498,210 in the Capital Outlay Revenue Limit and $7,339,107 in the Soft Capital Allocation for a total of $7,837,317. (See Attachment I)

Additionally, Bonnie selected the Mesa Unified School District as an example in order to prepare a sample growth calculation. As the sample shows, it follows the same logic as the M&O sudden growth calculation where columns which are negative will be subtracted from the total. Furthermore, in order for sudden growth to be allocated, the total for the fund must be greater than zero. Also, note the textbook amount of $69.68 for districts with high schools is included in the calculation. (See Attachment II)

RECOMMENDATION

The recommendation of this sub-committee is to:

- Provide all districts additional Capital Outlay Revenue Limit and Soft Capital Allocation monies in the current year to meet the needs and challenges of the current year growth.

- Apply the same law and rationale that is currently used to fund M&O growth to the Capital Outlay Revenue Limit and Soft Capital Allocation by creating a growth funding formula which would mirror that of the current M&O growth funding formula.

- Eliminate the minimum five (5) percent growth factor in the current Capital Outlay Revenue Limit calculation.

F I N A L D R A F T

ATTACHMENT I

CORL and SCA Growth Analysis

I. ASSUMPTIONS

a. Calculate growth in ADM for each grade level between FY04 and FY05

The 3 grade levels are: PSD
K-8
HS

b. Multiply each grade level growth amount (positive or negative) by each district's Capital Outlay Revenue Limit (CORL) and Soft Capital Allocation (SCA) support Level amount. (For High School, include the textbook support level amount.)

c. Add the three grade level totals and record value if total is greater than $0.00. If total is not greater than $0.00, set growth amount to $0.00

II. RESULTS

FY05 Calculated CORL Growth Assuming it was paid in FY05	$8,868,922.37
FY05 CORL Growth to be paid in FY06 (as of September 15, 2005) (CORL growth only if total FY05 student count exceeds FY04 by greater than 1.05) Data from APOR Tables	$8,370,712.82
Total Additional CORL Liability	**$498,209.55**
FY05 Calculated SCA Growth Assuming paid in FY06	**$7,339,107.71**
Total Potential Liability Increase for both CORL and SCA **(If paid in current year)**	**$7,837,317.26**

Stats

Total # of Districts in growth status for FY05 = 127

Total # of Districts eligible in FY05 to receive CORL Growth in amounts greater than:

$1000 = 113

$10,000 = 72

$100,000 = 26

In summary, there were 26 "High Growth Districts" eligible for/ in FY05 (Exclusive of SPED)

ATTACHMENT II

Arizona Department of Education

FY 2004 - 2005 CORL and Soft Capital Formula for Growth in Student Count

07-02-04 Mesa Unified School District APOR Date: 6/15/05

1. Unrestricted Capital Growth

	PSD	K-8	HS	Total
A. Current Year: 40th Day 100th Day (Unweighted ADM) Exclude all Charter School ADM	304.672	49,700.019	20,068.463	70,073.154
B. Prior Year 100th Day Student Count	308.625	49,656.514	20,014.700	69,979.839
C. Eligible Growth (Line 1A - 1B) 1 or 2 columns may be negative.	-3.953	43.505	53.763	93.315
D. CORL Support Level Amount From APOR 55-1 (Page 3 of 4) (For HS, Textbook Amt of $69.68 included)	225.76	225.760	337.620	
E. CORL Growth Amount	-$892.43	$9,821.69	$18,151.46	$27,080.72

2. Soft Capital Growth

	PSD	K-8	HS	Total
A. Current Year: 40th Day 100th Day (Unweighted ADM) Exclude all Charter School ADM	304.672	49,700.019	20,068.463	70,073.154
B. Prior Year 100th Day Student Count	308.625	49,656.514	20,014.700	69,979.839
C. Eligible Growth (Line 1A - 1B) 1 or 2 columns may be negative.	-3.953	43.505	53.763	93.315
D. Soft Capital Support Level Amount From APOR 55-1 (Page 3 of 4) (For HS, Textbook Amt of $69.68 included)	225.00	225.00	225.00	
E. Soft Capital Growth Amount	-$889.42	$9,788.62	$12,096.67	$20,995.87